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GPI - Q4 2011 GROUP 1 AUTOMOTIVE EARNINGS CONFERENCE CALL

EVENT DATE/TIME: FEBRUARY 09, 2012 / 3:00PM GMT

OVERVIEW:

GPI reported full-year 2011 consolidated revenues of $6.1b and adjusted diluted earnings per common share of $3.62. 4Q11 consolidated revenues were $1.63b, adjusted net income (excluding certain items) was $22m, and adjusted diluted earnings per common share was $0.94.

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Group 1 Automotive fourth-quarter earnings conference call. Please be advised that this call is being recorded. I would now like to turn the call over to Mr. Pete DeLongchamps, Vice President of Financial Services and Manufacturer Relations. Please go ahead, Mr. DeLongchamps.

Pete DeLongchamps - *Group 1 Automotive - VP Manufacturing Relations, Public Affairs*

Thank you very much, and good morning, everyone, and welcome to today's call. Before we begin, I would like to make some brief remarks about forward-looking statements and the use of non-GAAP financial measures. Except for historical information mentioned during the conference call, statements made by management of Group 1 Automotive are forward-looking statements that are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements involve both known and unknown risks and uncertainties, which may cause the Company's actual results in future periods to differ materially from forecasted results. Those risks include, but are not limited to, risks associated with pricing, volume and the conditions of markets. Those and other risks are described in the Company's filings with the Securities and Exchange Commission over the last 12 months. Copies of these filings are available from both the SEC and the Company.

In addition, certain non-GAAP financial measures, as defined under SEC rules, may be discussed on this call. As required by applicable SEC rules, the Company provides reconciliations of any such non-GAAP financial measures to the most directly comparable GAAP measures on its website. Participating with me on today's call are Earl Hesterberg, our President and Chief Executive Officer; John Rickel, our Senior Vice President and Chief Financial Officer; and Lance Parker, our Vice President and Corporate Controller. I will now hand the call over to Earl.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you, Pete, and good morning, everyone. Earlier today Group 1 reported record setting fourth-quarter and full-year operating results. Diluted earnings per common share on an adjusted basis were $0.94 and $3.62 for the fourth quarter and full year respectively. This was the best fourth quarter and best year the Company has ever reported since going public in 1997. What makes this particularly impressive is that we delivered these record results in a year where the overall industry selling environment was still weak at 12.8 million annual units and we had limited inventory availability from two of our key Japanese suppliers, whose brands normally represents about 49% of our new vehicle unit sales.

Even with our two largest manufacturing partners being constrained by natural disasters, our new vehicle unit sales grew 5%, demonstrating the resilience of our diversified brand portfolio and exceptional operating team. The unit sales increase coupled with higher average selling prices led to a 10.2% increase of new vehicle revenues. Used vehicle retail sales continued to be strong in 2011. Full-year revenues were up 11.4% on a 6.8% unit sales increase and a 4.4% higher average selling prices.

Finance and insurance revenues grew to a record $1,135 per retail unit resulting in a 16% revenue increase. We also reported a record fourth-quarter result of $1,183 per retail unit. These records can be attributed to the enhanced focus and oversight we put on this business that is driving better penetration rates of our product offerings. Parts and service revenues increased 6.1% in 2011 compared to 2010, reflecting increases in our customer pay, wholesale parts and collision businesses. We are very pleased that the work we have done in this business to improve processes, efficiencies and customer satisfaction have translated into increasing revenues and gross profits.

They outstanding growth in all of our business segments resulted in a 10.4% increase in total revenues to $6.1 billion and 9.5% higher gross profit in 2011 versus 2010. On a full-year basis, gross margin was 15.8%, reflecting higher new vehicle and used vehicle wholesale gross margins that were offset by slightly lower margins in our other business segments. Parts and service margins were down slightly to 52.3% as we experienced stronger growth in our tire sales, wholesale parts and collision businesses which have relatively lower margins, but drive customer retention, revenues and gross profit dollar increases.

Selling, general and administrative expenses were up 6.5% on an adjusted dollar basis, but our gross profit generation far outpaced this increase, which drove a 220 basis point improvement in our SG&A as a percent of gross profit to 76.4%. We're confident that the improvements that we have made to our underlying processes are sustainable and that we will continue to leverage our cost structure as new vehicle sales volumes continue to build over the next several years.

Operating margin improved 40 basis points year-over-year to 3.3% on an adjusted basis, again reflecting the improved operating cost structure. As I mentioned earlier, we had a record-setting profit year, even though we faced significant constrained vehicle supply issues from Toyota and Honda for most of 2011, due to the earthquake and tsunami that struck Japan in March and further exacerbated by a flood in Thailand later in the year. We're happy to report that our Toyota inventories are now about back to normal, and we anticipate that our Honda inventory should return to normal by the end of the quarter.

Speaking of supply and inventory, due to the lack of Toyota and Honda supply and our acquisition mix, our fourth quarter import brand mix decreased by about 5 percentage points from last year to about 50% of our new vehicle sales in the fourth quarter of 2011. The share was primarily picked up by our domestic dealerships which accounted for 20% of our units sales with the remainder from our luxury brands. Gaining share were Ford, GM, Chrysler, Mercedes Benz and Nissan Infinity. We anticipate that our import mix will gain some share back in 2012, as the supply issues we faced in 2011 recede.

New vehicle inventory grew 35% to 18,766 units from September 30, primarily driven by our import inventory increasing 46% to approximately 50 day supply during this same period. We ended the quarter with a 54 day supply of new vehicles, which is nearing our 60 day supply target. Used vehicle inventory increased from 29 days at September 30 to a 33 day supply at quarter end, well within our 37 day supply target.

Turning to acquisitions. We added six franchises to our portfolio in the fourth quarter that are estimated to generate about $218 million in additional annual revenues. And in January, we announced the acquisition of Hilton Head BMW in South Carolina and Volkswagen of Alamo Heights in San Antonio, Texas. These two franchises are expected to add approximately $93 million in annual revenues. As of today, we operate 143 franchises out of 111 dealerships in the United States and United Kingdom. I will now turn the call over to our CFO, John Rickel, to go over our fourth-quarter financial results in more detail. John?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Thank you, Earl, and good morning, everyone. Per diluted common share, adjusted net income improved 51.6% over prior year to $0.94, which is the best fourth-quarter results in our Company's history. What makes this result even more impressive is that we achieved these levels in a 13.4 million SAAR selling environment that continued to be constrained by Japanese inventory shortages and a weakened economy. In comparison, the next best fourth-quarter results were achieved in a SAAR environment of 16.8 million units. This reflects the significant improvements we've made to our processes and cost structure and begins to demonstrate the leverage those improvements will deliver as new vehicle sales volume increases over the next few years.

Our net income for the fourth quarter of 2011 rose $7.3 million, or 49.3% over our 2010 results, to $22 million on an adjusted basis. These results for 2011 exclude $461,000 of after-tax, non-cash asset impairment charges as well as a $641,000 after tax charge related to an accrual for a pending legal matter. The comparable prior period results excludes $4.9 million of after-tax non-cash asset impairment charges, as well as an $810,000 income tax benefit related to discrete items. Compared to the same period a year ago, our adjusted operating margin improved 40 basis points to 3.2%, and our adjusted pretax margin improved 50 basis points to 2.2%.

On a consolidated basis, revenues increased during the fourth quarter by $188.2 million, or 13.1%, to $1.63 billion, compared to the same period a year ago, reflecting increases in each of our business segments. New vehicle revenues increased 13.5% to $945.4 million on 8.1% more units to the ongoing effects of supply shortages in a number of our Japanese brands were more than offset by improved sales in our major domestic brands. In addition, our average new vehicle sales price improvement by 5% to $34,448 per unit. Our used vehicle retail revenues increased 16.8% to $362.9 million on 12.7% more units and a 3.7% improvement in our average used vehicle retail sales price per unit. Used vehicle wholesale revenues grew 0.9% to $59.4 million while our F&I revenues rose 20.8% to $53.5 million, or $1,183 per retail unit sold. This represents our best quarter ever for F&I PRU. And for the eighth straight quarter, we reported year-over-year revenue growth from the core of our business, the parts and service segment.

Revenues from the parts and service business improved $13.5 million, or 7% to $204.7 million. Our gross profit increased $28.8 million, or 13.3% from the fourth quarter a year ago, to $245.9 million, which included increases of 23.6% in new vehicles, 16.2% in total used vehicles and 4.6% in parts and service, as well as the F&I improvement that I just mentioned. Overall, our gross margin remained flat compared to the fourth-quarter a year ago at 15.1% as continued strength in our F&I business and improved new vehicle retail gross margins were offset by the mix effect of increases in our new and used vehicle business, as well as declines of 20 and 130 basis points in our retail used vehicle and parts and service segments respectively.

We continue to leverage our cost base, and as a result, SG&A expenses as a percent of gross profit improved 260 basis points to 76.1%. Floorplan interest expense declined $1.4 million, or 16.3% from prior year, to $7.4 million. This decrease reflects declines in both the weighted average floorplan borrowings during the quarter, as well is the weighted average interest rate. The weighted average interest rate was positively impacted in this quarter by the expiration of interest rate swaps in December 2010 and in August 2011. At December 31, 2011, our new vehicle inventory stood at 18,800 units with a value of $619.2 million compared to 18,700 units with a value of $572 million a year ago.

Our import brand inventory levels improved toward the end of the fourth quarter, closing at 50 day supply. Luxury and domestic brand new vehicle inventory closed the year at 39 and 83 day supply, respectively. Manufacturers' interest assistance, which we record as a reduction of new vehicle cost of sales at the time the vehicles are sold, covered 98.2% of total floorplan interest expense in the fourth quarter, which is up from 69.3% in the fourth quarter a year ago and up 140 basis points from the third quarter of this year. Other interest expense increased $2 million, or 28.2% to $8.9 million, primarily explained by increased mortgage borrowings associated with recent acquisitions and higher mortgage interest rates. Our consolidated interest expense includes non-cash discount amortization of $2.4 million related to our convertible notes.

For the full year of 2011, we also generated an all-time record for adjusted net income of $3.62 per diluted common share. Again, these results are all the more impressive when considered in the context of the 2011 selling environment that is down about 25% from our next best year. Our consolidated revenues were $6.1 billion, which was up 10.4% from the 2010 results. New vehicle unit sales rose 4.6% to $102,022 units, while used retail vehicle unit sales increased 6.8% to 70,475 units. Total gross profit improved 9.5% to $960.6 million, included an 18.3% increase in our new vehicle gross profit, an 8.3% improvement in our used vehicle retail gross profit, a 16% rise in F&I, and a 3.2% increase in our parts and service gross profit. Adjusted SG&A expense as a percent of gross profit improved 220 basis points to 76.4% while our adjusted operating and pretax margins both rose 40 basis points to 3.3% and 2.3% respectively.

Now, turning to the fourth quarter same-store results. In the fourth quarter we reported revenues of $1.53 billion, which was a $92 million, or 6.4% increase from the comparable 2010 period. Within this total, new vehicle revenue was up 6.3% to $883.3 million on 1.4% new -- more new vehicle retail unit sales as improvement in our domestic brands helped to offset the shortages of Toyota and Honda inventory that continued to challenge us during much of the fourth quarter. Those inventory shortages, coupled with a continued shift in car truck sales mix back toward trucks, contributed to an increase in our average new vehicle sales price of $1,582 per unit to $34,385.

In total, our used vehicle revenues rose 8.8% to $400.6 million on 2.2% more units. Our used retail revenues improved 11.3% to $344.8 million on 71.1% more units and a $770 increase in our average retail used vehicle sales price to $20,476. Our wholesale used vehicle revenues declined 4.5% to $55.8 million on a 6.6% decrease in unit sales. Our F&I team produced another record quarter as F&I income per retail unit rose 10.1% to $1,184, driven primarily by increases in our income per contract and penetration rates for our major product offerings. In total, F&I revenues were up $6.2 million, or 14% compared to the same period a year ago.

We posted another solid quarter in our parts and service business. Parts and service revenues grew 0.5%, which is more than explained by increases of 3.2% in our customer pay parts and service revenues, 5.7% in our wholesale parts business and 6.6% in our collision business. Our customer pay revenues improved in most of the major brands that we represent as initiatives focused on customers, products and processes continue to build momentum. Our wholesale part sales continued to benefit from the closure of competing dealerships in the stabilizing economy that has helped to strengthen the credit worthiness of our wholesale parts customers.

Improved business processes in our collision segment continued to produce positive results. Partially offsetting these positive results was a 14.3% decline in our warranty parts and services revenues resulting from the drop-off of several large recall campaigns that bolstered prior year results. Specifically, warranty parts and service revenues from our Lexus brand stores declined more than 50% while Toyota warranty revenues were as over down 25% from prior year. Overall, our gross profit improved $15.9 million, or 7.3%, and our total gross margins improved 10 basis points over prior year to 15.2%, primarily reflecting the strength of our new vehicle and F&I performance. Compared to results a year ago, our same-store new vehicle gross margin improved 50 basis points to 6.1%, which is primarily the result of a rise in gross margins in our luxury and import brands. And our total used vehicle margin improved 10 basis points to 6.9%, reflecting a slight increase in the percent of used units acquired by a trade-in.

Our parts and service margin declined 40 basis points to 52.6%, primarily reflecting the mix effect of our growing collision and wholesale parts business, which on a relative basis generates lower margin than our customers pay and warranty parts and service businesses. We continue to leverage our cost base. Our adjusted SG&A as a percent of gross profit improved 250 basis points to 75.9%. As new vehicle sales increased and gross profit continues to grow, we would anticipate further leveraging SG&A. A rough rule of thumb is that we expect that each incremental gross profit dollar will only add about $0.50 to SG&A expenses. On an adjusted basis, our same-store operating margin improved 40 basis points to 3.2%.

Now, turning to liquidity and capital structure. During the fourth quarter of 2011, we had generated adjusted cash flow from operations of $34.4 million. For the full-year, adjusted cash flow from operations totaled $152.3 million. As of December 31, 2011, we had $14.9 million of cash on hand and another $109.2 million that was invested in our floorplan offset account, bringing immediately available funds to a total of $124.1 million. In addition, we had $225.7 million available on our acquisition line that can also be used for general corporate purposes. As such, our total liquidity at December 31, 2011 was $349.8 million. We used $17.9 million for capital expenditures during the quarter to construct new facilities, purchase equipment and improve existing facilities, which brought our total CapEx for 2011 to $40.1 million.

With regards to our real estate investment portfolio, we own $444.2 million of land and buildings at December 31, which represents approximately one-third of our total real estate. To finance these holdings, we've utilized our mortgage facility and executed borrowings under other real estate specific debt agreements. As of December 31, we had $41 million outstanding under our mortgage facility and $188.3 million of other real estate debt, excluding capital leases. For additional details regarding our financial condition, please refer to the schedules of additional information attached to the news release, as well as the investor presentation posted on our website. With that, I'll now turn back over to Earl.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thanks, John. If you'd asked us back in 2007 how we would expect to perform in a 12.8 million unit new vehicle selling environment, we would've anticipated being close to breakeven. So, we are delighted that we not only reported strong financial results for both the fourth quarter and the full year, but record-setting financial results. I'm proud of the job our operating team has done in restructuring our business, significantly improving processes, delivering on growth and keeping our customers satisfied.

We are very optimistic about the future. We expect significant and steady growth in the industry over the next few years with an increase to 14 million units for the industry in 2012. Driving sales in the coming years is significant pent-up customer demand as evidenced by the record age of the US car park that is nearing 11 years. The increased marketing spend we are seeing from our manufacture partners, customer financing that is back to pre-recession conditions, balanced inventory levels, strong used car values and many new exciting product launches.

With the improvements we've made, we are confident we will be able to continue to leverage our costs and deliver earnings growth in such an environment. Capital expenditures are projected to be less than $55 million in 2012, with $15 million of that total dedicated to specific parts and service growth initiatives. While we have not set a specific target, we do expect to remain active on the acquisition front. We continue to actively seek deals in the United States and the United Kingdom that meet our strategic and financial targets. With the strongest balance sheet in the sector, we're well positioned to continue to grow the Company and build scale while adding value for our shareholders.

That concludes our prepared remarks. I'll now turn the call over to the operator to begin the question and answer session. Operator?

QUESTIONS AND ANSWERS

Operator

We will now begin the question and answer session. (Operator Instructions). And our first question will come from Himanshu Patel of JPMorgan. Please go ahead.

Rick Alo - *JPMorgan - Analyst*

Yes, hi, this is [Rick Alo] for Himanshu Patel this morning. I have a quick question on your incremental throughput. I know you guys have a target of $0.50 of incremental throughput on future gross profit growth. But I just wanted to understand what would that number be, including acquisitions? Because particularly this quarter, this number including acquisitions was 40%.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Right, this is John Rickel. The rough rule of thumb that I gave you of kind of $0.50 flow through is on a same-store basis. So, you are right, when you throw in the acquisitions it was below that, but if you adjust for the acquisitions impact, it was more like $0.52. So, we continue to be very comfortable with that rough rule of thumb that we've shared with you.

Rick Alo - *JPMorgan - Analyst*

Okay. Sure, and in terms of acquisitions, we have noted that in the last one year, all the acquisitions that you guys have made were -- are targeted to premium -- to luxury and domestic luxury customers. And is that just an attempt to diversify or expose it away from Japanese auto makers maybe? Or is that is true what is the mix that you are -- you guys are expecting in future in terms of domestic luxury and Japanese luxury?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes, this is John Rickel. Let me correct you on the specifics, and I'll let Earl address the strategy question that really underlies that. What we acquired last year included domestic. So, Ford, GM, there were both domestic and some luxury brands in there. And I'll let Earl kind of address the broader question.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes, I think we're now in an environment where I no longer limit or specifically target the brands that we would consider going forward in terms of acquisitions. The strength in terms of sales growth last year, certainly at the end of last year, was with the domestic brands. We purchased a couple last year, so now we are merely looking for acquisitions that are good return on investment for our shareholders and hopefully that supplement the scale we may have in specific geographic markets. So, I would say we are more open on the brand mix of acquisitions than have we ever been, at least since I've been in Group 1.

Rick Alo - *JPMorgan - Analyst*

Okay, sure, and the last question will be on your new weaker margins. I saw your margins coming down pretty sharply this quarter on a sequential basis, at least. How -- what would you attribute that to, and going forward, how should we think about weaker margins? If you could share some color on that.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes, this is John Rickel. We had indicated all along that the margins that we drove in kind of the second and the third quarter benefited pretty sharply from the overall industry inventory shortages. We are overweight on Toyota and Honda, and with those brands in particular being in short supply through the summer months, our operating team did a good job of fully maximizing the value of our inventory. As the inventories have come back, we have said all along that we anticipated those margins return into more normalized levels, which is really what you saw in the fourth quarter. On a year-over-year basis we were up, but you are right, sequentially, we were down. And we would anticipate as inventories have normalized that you're going see something probably in that low 6% range as we go forward.

Rick Alo - *JPMorgan - Analyst*

Okay, sure, thanks a lot.

Operator

Our next question comes from John Murphy of Bank of America Merrill Lynch. Please go ahead.

John Murphy - *BofA Merrill Lynch - Analyst*

Good morning guys, can you hear me?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes. Hello, John.

John Murphy - *BofA Merrill Lynch - Analyst*

Just a first question on pent-up demand for Toyota and Honda. You seem to indicate that these three were really making up for the weakness in those two brands, just given the inventory shortages in the fourth quarter. I was just curious, as we step forward and those inventories are normalized as you are indicating first and second quarter, if you think there will be a bit of a snap back over at least a pent-up demand for those brands. Or has that been fulfilled by sort of competing brands? Just trying to understand really the pent-up demand for those two brands specifically.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

John, it's Earl. I don't know that I would attribute a massive pent-up demand. I think -- I don't think a lot of customers would hold off and wait when they need to buy a new car these days. So much of the replacement demand is just driven by the age of the car park. But do think that there's some optimism for Toyota and Honda in that they have more inventory available. They're very powerful companies and powerful brands who will fight to regain sales. I think we've already seen some evidence of that, and they now start to have some new product available, which gives them an avenue to flex their marketing muscle., which they both have. So, the new CRV came out before Christmas. Toyota has many product launches this year, obviously, the Camry launch was the fourth quarter last year and it appears to be building momentum. So, I don't know pent-up demand is a big element of the optimism I would feel about Toyota and Honda, but I think they've -- there is a lot of reason to believe they're going to be get some share back this year.

John Murphy - *BofA Merrill Lynch - Analyst*

That's helpful. Then just the second question on pricing. It sounds like you are saying that Toyota and Honda are getting a little bit more promotional, yet we are seeing average transaction prices rise pretty significantly throughout the industry. I'm just curious what you're seeing there. Are there sort of fewer stair step programs that are going on behind the scenes that are not being captured in published data? Just trying to understand the increase in the marketing dollar, whether they're on the ad spend side or whether they are actually on the incentives?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

I haven't seen a lot of price driven marketing yet by Honda and Toyota, and nor have they needed it because of their inventory situation. So, I don't think their marketing thrust has really been priced to date, nor have -- they have been a recent heavy user of stair steps. But I don't know what would happen in the future, but I know there will be a lot of competitive market activity this year to launch new products to promote the brands. And how much of it escalates in terms of marketing spend, I don't know, but I think it will be a good year to buy cars for consumers. The best one in a couple of years.

John Murphy - *BofA Merrill Lynch - Analyst*

Talk about marketing dollars. I mean, really, that could be toggled between ad spending and incentives. Is that correct?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes, that's right, and that's kind of a tactical thing that the manufacturers decide quarter by quarter basis. I mean, you saw the money spent on the Super Bowl the other day. There were quite a few car ads on that, so I think that is a precursor that the marketing budgets are in play for the OEMs. And most of them have some new product this year that they want to position in the market.

John Murphy - *BofA Merrill Lynch - Analyst*

And as we all know, it's only half time in America.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

(laughter). I believe I saw that one too.

John Murphy - *BofA Merrill Lynch - Analyst*

We all have. One last question, you spent a little bit of time at the data convention last week, and it sounds like there is a lot of buzz and potentially availability of acquisition for stores for sale. In some cases, it sounds like you may be just a little bit more than onesies and twosies that in the next year or two might be some big groups that they could potentially be up for sale. I'm just curious if you would be open to a large acquisition, or are you comfortable doing sort of these smaller tuck-ins over time?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

No, we would always prefer a larger acquisition. I just think the more scale you get in a given market, which is usually what you get with a larger acquisition, is better for us. So, we are completely open to larger acquisitions.

John Murphy - *BofA Merrill Lynch - Analyst*

Okay, great. Thank you very much, guys, keep it up.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you.

Operator

Our next question comes from Simeon Gutman of Credit Suisse. Please go ahead.

Simeon Gutman - *Credit Suisse - Analyst*

Thanks, and good quarter and year. A question on expenses. You had a great performance pretty much all year. Can you talk about the areas of the business that gain efficiencies? How should we think about them potentially accelerating throughout 2012?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes Simeon, this is John Rickel. The pieces really were around leveraging the scale, so it's things like the fixed cost. You obviously don't add more rent or store costs for a given level of volume. So, as we have been able to drive grow profit dollars, we leverage that. The team has done a good job of continuing to be appropriately restrained with advertising. You obviously need to accelerate it as the volumes come up, but they are not out accelerating what is going on there. I think we've done a good job on the fixed part of personnel. If you think about accounting cost, payroll cost, those are not linear with volume either, and I think we have done a good job of scaling those. So, it's really about driving, for a lack of a better term, more revenue through those fixed cost elements has really given us the leverage.

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Simeon Gutman - *Credit Suisse - Analyst*

Okay, and then on the same-store gross profit in parts and service on the same-store basis. I think those numbers are a little challenged, but some of that is tough compare, some of it may be mix. Can you talk about first when the warranty compares, when they ease? And then how we should think about the same-store gross profit and outlook for the parts and service business over the course of the year?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes, this is Earl. Clearly, fourth quarter last year was one of our worst comparator numbers on warranty because Toyota Lexus recalls were really somewhere near their peak back then. I believe it will be close to third quarter before some of those comparisons ease up. With our warranty business down over 14% in the fourth quarter last year, that was a huge hit. And -- but that will ease as we certainly move into the second half of 2012, in terms of the degree of difficulty of the comparison.

Simeon Gutman - *Credit Suisse - Analyst*

Okay, and then last one on F&I for vehicles, it's a pretty chart for the whole year. Can you talk about, I don't know how the J3 supply situation may have had an impact or if they are just -- are there new products you're selling, other technologies or the price and any other mix implications?

Pete DeLongchamps - *Group 1 Automotive - VP Manufacturing Relations, Public Affairs*

Simeon, it's Pete DeLongchamps, and thank you for your kind words. It was really function of us focusing on penetration rates and identifying dealerships that had opportunity. And there were certain regions of the country that we traditionally did not perform well, and our field staff really improved the processes, redoubled our efforts on training. And we just got great results from select dealerships in markets that made a significant difference on the overall PRU.

Simeon Gutman - *Credit Suisse - Analyst*

Is there a target amount per vehicle that if you go through the benefits you have been seeing, that we should think about? And then, as a supply comes back and some of the import volume mix is back in, how should that play into the per vehicle number?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

It's almost impossible -- this is Earl, by the way, to lock into a target number. The market is very dynamic, particularly as lease programs come and go, they change our ability to penetrate in various brands and geographic markets. I think the only thing we can say is we think we have upside from here. We think we can continue to take that number up a bit.

Simeon Gutman - *Credit Suisse - Analyst*

Okay, and just connected to that, are you seeing the quality of offerings change? Or they're the same, you're just executing better?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Well, we are executing better, but we have to also agree that it's a better financing environment. And obviously, finance income is a big part of this business equation. So, as banks are more aggressive at lending, more customers finance., and that helps this business equation. And as consumers are a little more optimistic and willing to step out and commit to products and loans and things, that helps this process also.

Simeon Gutman - *Credit Suisse - Analyst*

Okay, thanks.

Operator

Our next question comes from Nick Nelson of Stephens. Please go ahead.

Rick Nelson - *Stephens Inc. - Analyst*

It's Rick Nelson, thanks, and good morning.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Good morning, Rick.

Rick Nelson - *Stephens Inc. - Analyst*

Congrats on a great quarter and year. Same-store unit growth for new cars up 1%. It looks like it lagged the industry. Wondering if you could comment there. Was it the inventory shortages? And if you can comment on market share within your margins.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes, certainly, Rick.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes, it was driven almost entirely just by a lack of availability in about half of our business, which is Toyota, Lexus, Honda, Acura. And there's also some shortages in BMW. We sold out of X3s and X5s for a long time, and we'd run down 3 series. So, it's not just the Japanese brands, but there are some other brands that have been short of product as well.

But I'll give you an example, at our biggest Lexus store in the last few days of December there were four model lines. We had nothing to sell. Nothing. And even in our big Toyota dealerships, and we have 2 of the top 10 in the country, we thought we had restocked nicely and had enough inventory going into December. By the end of December we were out of several model line of cars. And so we did not finish the fourth quarter as strongly as we would normally in our Japanese brands. So, I believe that explains the issue. So, we're looking forward to outpacing the industry average gross -- growth in new vehicle sales this year. I mean, we need to -- just like Honda and Toyota need to recover, we need to get on that bandwagon with them this year.

Rick Nelson - *Stephens Inc. - Analyst*

I know it's a small piece of your business, but if you could comment on the UK, how that performed in the quarter.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes, the UK business, we are fortunate. We are with BMW and Mini there, it is about 5% of our sales. BMW and Mini are two of the strongest brands in the UK at the moment and throughout last year. The UK market showed to be down 4.4% last year, but that was overstated a bit because the actual retail business in the UK, the selling cars to customers one at a time was down about 14%. So, there's no doubt the UK economy is weak and the UK auto business is struggling. However, the premium brands, as you might expect, like BMW and Mini and others, are holding up significantly better. But there's nothing positive about the UK economy at the moment, relative to auto retailing.

Rick Nelson - *Stephens Inc. - Analyst*

And on the acquisition front, $563 million at revs for the year. You are off to a big start in 2012. Can you comment on acquisition pricing and with the recovery and auto sales tending to be firmly in place, how the sellers is willing to part with their dealerships?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

It is still quite challenging to find acquisitions that fit our investment return hurdles. It's still very difficult. You look at it incredible number of opportunities to find one. Clearly, the ones we found will meet our 15% pretax return on investment hurdle, or we would not have done them. But it's -- there is more to look at, but it's no easier to do a deal now than it probably was at this time last year. Real estate makes it more complicated, because commercial real estate values have obviously dropped since the recession began in 2008 or late 2007. So, people who have been in real estate for a long time, that is difficult for them to come to grips with current market prices on real estate sometimes.

Rick Nelson - *Stephens Inc. - Analyst*

How would you rank the capital alternatives at this point? At acquisitions, buy backs or at retirement?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Clearly, our priority is to grow our Company in acquisitions or investing in expanding our business through our additional stores. So there's -- that is number one. One A, B, C and probably number two.

Rick Nelson - *Stephens Inc. - Analyst*

Okay (laughter). Terrific, thanks a lot, and good luck.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thanks, Rick.

Operator

Our next question comes from Ravi Shanker of Morgan Stanley. Please go ahead.

Unidentified Participant - *Morgan Stanley - Analyst*

Good morning, everyone. This is EJ in for Ravi. Just a couple of quick questions if I can. You guys have guided to a $14 million SAAR for 2012, sort of on the back of strong, you know, the old car fleet and budgets. You guys alluded to bigger ad budgets. Do you guys see any potential for upside to that now that we have sort of printed a 4 point -- 14.2 in January? Or is that sort of more of a ceiling?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

I think there is a potential upside for that. I wouldn't forecast that there is too much uncertainty in the world. It seems like something positive happened in Greece today. But there is just too much uncertainty around the globe, and it's now a global economy, and things anywhere in the globe can, you know, within a half hour affect the US consumer sentiment. So -- but we're -- $14 million, I think is certainly a credible number when you look at how the fourth quarter finished last year, how January started this year. And when we see that age of these trade-ins that are coming into our dealerships, a lot of old cars being turned in. So, I feel pretty good about $14 million, and I don't think it's a ceiling.

Unidentified Participant - *Morgan Stanley - Analyst*

Got it. If I could switch gears a bit into used, seems like used inventory appears to be still pretty tight and acquisition still pretty high. And we're anniversarying into sort of a sort of trough period for those off-lease vehicles. How do you expect that to play out in 2012 for you guys? And can we continue to exceed these -- expect to see these depressed used margins?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes. It's still hard to find good used cars. We are getting more trade-ins of the as the new vehicle market improves, new vehicle sales improves. But as I just mentioned, the age of some of these trade-ins, many of them are not really retailable. Or they are low dollar units that don't hit that fat part of our target market for used vehicle retail. So, I think that the used car pricing will probably stay firm this year and it's still going to be a challenge to get enough high-quality used cars for retailers such as ourselves.

Unidentified Participant - *Morgan Stanley - Analyst*

Great. If I could sneak in one more. I didn't hear anything about this previously. Do you guys -- could you guys give a bit more color surrounding the nature of the pending legal matter that you guys had this quarter?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

No. We can't comment on the litigation. It's a very unusual and complex matter. But I think as it relates to our investors and probably to you and your colleagues, the worst-case financial impact to our Company was accounted for in the fourth quarter of 2011. So, it's already included in our financial statements. So financially, that should not be a matter going forward.

Unidentified Participant - *Morgan Stanley - Analyst*

Okay, great thanks so much, guys.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you.

Operator

Our next question comes from Aditya Oberoi of Goldman Sachs. Please go ahead.

Aditya Oberoi - *Goldman Sachs - Analyst*

Hi, guys.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Hi.

Aditya Oberoi - *Goldman Sachs - Analyst*

I had a quick question on your overall sales in the fourth quarter. Can you talk a little bit about specific regions you saw more strength versus others?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes. This is John Rickel. We saw really good strength in Texas and Oklahoma again. That part of the country did quite well. Gulf Coast was pretty decent. Some weakness up into kind of the Northeast. For us, though, that's hard to separate between that and brands that was --we are pretty heavy in import up to Boston area, for example. And as Earl indicated, we continue to suffer from inventory shortages. And similar, sort of, in California. A little bit weaker there, but we are very heavy in import out there as well. So, for us, it's a little hard to sort geography from the inventory shortages issues. But certainly, Texas and Oklahoma had a very good quarter.

Aditya Oberoi - *Goldman Sachs - Analyst*

Great. And one question on the PNS. Obviously, you were lapping tough comps so that -- and then warranty was a headwind this quarter, so PNS same-store sales was only up 0.5%. As you think about 2012, warranty will continue to be a headwind. What kind of growth should we be thinking about in that specific segment?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes, this is John Rickel. I think we're still comfortable, kind of low single digits in that area.

Aditya Oberoi - *Goldman Sachs - Analyst*

Okay. And do you think -- obviously that will come after the cost of a small headwind to margins, given that the mix would be more towards, as you said in this quarter as well will be tires and other low margins product?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Yes, I think -- this is John again. I think that's fair, but I don't think that's huge amounts of margin degradation. But yes, there's probably a little margin pressure that may be in there.

Aditya Oberoi - *Goldman Sachs - Analyst*

Great, thanks a lot, guys, and congrats on a good quarter.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Thank you.

Operator

Our next question comes from Brad Hoselton of KeyBanc. Please go ahead.

Matt Mashon - *KeyBanc Capital Markets - Analyst*

Hey, this is [Matt Mashon] in for Brett.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Good morning.

Matt Mashon - *KeyBanc Capital Markets - Analyst*

Good morning, how are you? Used as a percentage of new slipped in the fourth quarter to 65%. As sales rise next year, are you -- would you expect to be able to keep up with the new sales or the used, or would you expect that ratio to decline little bit?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

I don't really manage that ratio, so I don't know. That ratio is so dependent on our geographic mix of sales because of places like California and the Northeast where we don't have space for lots. So, we don't really manage to that ratio number because for us, it's not meaningful.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Right, but I would -- this is John. I would anticipate, given areas that Earl mentioned tend to be our big import areas. We're going to -- should see kind of more new vehicle growth there as the Toyota and Honda inventory situations improved. And that would lead me to logically say there probably is some pressure on that new to used ratio, because we're going to likely grow new vehicle sales faster than what they pick up their used vehicle sales because of the space limitations.

Matt Mashon - *KeyBanc Capital Markets - Analyst*

And on SG&A incremental. Your targeting or rule of thumb is $0.50 on the dollar. Is -- what would drive -- what would be kind of a headwind to that? What would be kind of a tailwind to that? Is there anything we should be about 2012 versus 2011?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

No. We continue -- this is John. We continue to be comfortable with that rough rule of thumb. And remember, that is on a same-store basis. But no, I think that that's a reasonable calculation basis for your models.

Matt Mashon - *KeyBanc Capital Markets - Analyst*

And then just follow-up on the acquisition activity, in particular in the UK. You saw Penske make a larger acquisition there. Has maybe some of the issues over in Europe created some opportunity there?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Yes. I think any time a market is under financial pressure, economic pressure, that there are some opportunities for acquisitions to come out of that. So, I'm optimistic that we will be able to look at some things in the year ahead that we haven't had a chance to look at in the past couple of years.

Matt Mashon - *KeyBanc Capital Markets - Analyst*

Thank you very much.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you.

Operator

Your next question comes from Scott Stember with Sidoti Company. Please go ahead.

Scott Stember - *Sidoti & Company - Analyst*

Good morning.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Good morning, Scott.

Scott Stember - *Sidoti & Company - Analyst*

Can you talk about how your luxury premium brands did, specifically BMW and Mercedes?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

BMW was fantastic all year for us, and they are a bigger part of our mix than Mercedes is. In fact, as I mentioned, we have been constrained, as most BMWs have been, on X3s and X5s all year. And as we sell down the 3 series, they're just about to launch the new 3 series, we probably could have done even better. But BMW was fantastic in the fourth quarter and all year, even with limited supply. And I will say that we have six Mercedes stores and a couple big ones. Mercedes came on very strong in the second half of last year, and the M class SUV for them was very powerful as the year came out. So, we saw in Mercedes on an upswing at the end of last year also.

Lexus, just we did not have any bullets. Just did not have the vehicles to sell and actually, still don't. Still don't. And hopefully, that will build this first quarter. But I think that when Lexus has product, they will increase sales again too.

Scott Stember - *Sidoti & Company - Analyst*

All right, and on mid-level imports going over to Honda. Can you talk about how the new Civic performed in the quarter? And now with a refreshed model coming out in the next few months, what are your expectations on any sales hiccups going forward?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Well, I think we are going to see positive numbers for Honda throughout most of this year. I don't know that the Civic's going to be a huge factor. But a comparison we started to get into some getting to comparisons as we get into the spring and summer against the very weak months last year. And the CRV is bringing a lot of Honda traffic back into the dealership. So, I don't think Honda will be a spectacular story, but I think Honda will display some steady growth numbers this year that will probably peak near the end of this year.

Scott Stember - *Sidoti & Company - Analyst*

Okay. The just the last question, a follow up on acquisitions. Earl, you mentioned focusing more on returns versus brands. But how does the Chrysler brand fall into your thought process going forward?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Well, not sure I'm 100% convinced yet. But I have to tell you, our Chrysler dealerships did good last year and our Chrysler were up like around 50, 5-0% last year. So, it does catch your attention. Those are all obviously very low comparator months and year. But our Chrysler dealerships were a pleasant surprise last year. The sales growth is big.

And never say never, hasn't made it at the top of the list yet. But didn't think we'd ever have this type of conversation where I could say Chrysler sales were up 50% either. So, that Company has really done a lot of things right. So, it would have to be a really attractive investment opportunity for our Company. But never say never.

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

It's only halftime.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

(Laughter) It's only halftime.

Scott Stember - *Sidoti & Company - Analyst*

Fair enough, that's all I have, thank you.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Okay.

Operator

Our next question comes from James Albertine of Stifel Nicolaus. Please go ahead.

James Albertine - *Stifel Nicolaus - Analyst*

Great, thank you, and good morning. Thanks for taking my question, and congratulations on a strong quarter. I guess the first thing I wanted to touch on very quickly was just any sort of color you can provide from a regional perspective on parts and service, given warmer than average weather and in general, customers sort of deferring service work. We're seeing that across the after market, certainly, but wanted to understand the impact that you are seeing on your businesses. And then secondly, you do a lot of what I think is great work on customer tracking. And so, what can you glean from the data you've collected in the back half of last year in terms of perhaps, are customers taking a longer time to research new purchases? Are they simply just buying cars when their existing cars are becoming undrivable? What trends have you sort of noticed there that you can give us some insight into? Thanks.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

That's a great question, actually. First to your parts and service question, I don't have a much insight regionally. We haven't seen much difference regionally, although we are starting to pick up anecdotal bits about, oh, we're not having a harsh winter in the Northeast and so forth. I guess we'd have to have first quarter data and compare it to last year. But there's -- clearly, we are not getting the snow, and if we don't get snow in February or March, there will be a little -- some collision business issues up over prior year in the Northeast. But our collision business is spread across the country pretty evenly. We are seeing, I would say, with service customers that -- and for the last couple of years, it's been hard to sell some of the maintenance type work such as a brake job or something. They'll put that off as long as possible. But then on the repairs we do get in the dealership, they have to be done, and they tend to be some nice, you know, bigger dollar repairs. Because people have to keep these cars running and when they need repair, it needs significant repair. And I expect the after market has been seeing that type of thing also. And I don't think the economic pressure has eased up that much in terms of that dynamic in the parts and service business.

Your point on the new vehicle purchases, I would say that customers are much -- doing a lot more shopping before they enter the dealership using the Internet. Very well-versed in the products they are considering in terms of the technology and the product offerings. So, it does put a lot of pressure on us to keep up the training of our salespeople and make sure that, you know, we can continue to provide service and not be at a disadvantage versus a well-educated customer. And that's something we are working on in our Company, is that training aspect. And I think that's all pretty logical in an environment like this. So, I think there is some data relative to Internet shopping that supports that.

James Albertine - *Stifel Nicolaus - Analyst*

Great, thanks so much, and just a quick follow-up to your last point there. I would think that, it just makes sense to me that in this environment, a Company like yourselves with a larger consolidated footprint and a healthier balance sheet to some extent to make investments in technology and improvements in technology and customers facing interactions, you'd stand to gain market share from perhaps a small mom-and-pop, if you will. Is there any sort of color you can provide there?

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

For competitive reasons, I don't want to go into too much detail, but absolutely. We, through last year and accelerating into this year, we have a lot of technology investments we are making in areas like customer relationship management, social and digital media and things like that. And customer handling related things. So, yes. That is one of the advantages that we should have as a big group is technology -- bringing technology to improve customer satisfaction, but also to make our people more productive and efficient. So, we're definitely have some significant technology investments underway.

James Albertine - *Stifel Nicolaus - Analyst*

Great, very helpful, thanks for your help.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you.

Operator

Our next question comes from [Ken Revlen of [Urbacon Partners]. Please go ahead.

Ken Revlen - *Urbacon Partners - Analyst*

Good morning, gentlemen, great quarter.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thank you.

Ken Revlen - *Urbacon Partners - Analyst*

Quick question for you. The $12 million in amortization of debt discounts for 2011. I just wanted to confirm in that almost all of it the non-cash amortization due to the convertible notes, is that correct?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

Absolutely. This is John.

Ken Revlen - *Urbacon Partners - Analyst*

So, this is another, something like $0.50 in cash per share, so, and if you look at the adjusted earnings, it is more like $4.10 than $3.60 if you add that back, right?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

That is correct. If we hadn't had to deal with APB 14-1, that is spot on.

Ken Revlen - *Urbacon Partners - Analyst*

Right, okay. And the other question I had, I think maybe it was a year ago, maybe couple of years ago. And you provided this interesting (inaudible) when it came to EPS versus 1 million incremental SAAR. And it used to be something like $0.55 to $0.65. What is your current thought on that? Is that kind of like still on the low end of that?

John Rickel - *Group 1 Automotive Inc - SVP, CFO*

No. I think, especially when you factor in things like APB-14-1, thinks like that, we've kind of adjusted that to an expectation of kind of $0.50 to $0.55 of EPS for everyone million units in SAAR change.

Ken Revlen - *Urbacon Partners - Analyst*

Okay, okay. So, that was on the same ballpark. Great, that's all I had, thanks very much. Thank you.

Operator

This does conclude our question-and-answer session. I would now like to turn the conference back over to Mr. Hesterberg for any closing remarks.

Earl Hesterberg - *Group 1 Automotive Inc - President, CEO*

Thanks to everyone for joining us today. We look forward to updating you on our first quarter earnings results in April. Have a good day.

Operator

The conference is now concluded. Thank you for attending today's presentation, you may now disconnect.
